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MOST COMMERCIAL FARMS NOT EXPERIENCING STRESS

Allan E. Lines
Associate Professor
Agricultural Economics and Rural Sociology
The Ohio State University

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Farm sector incomes and cash flow in 1986 rose substantially over 1985 levels due largely to lower costs of agricultural inputs and government payments. However, financial stress in some segments of the farm sector continued. Stress for purposes of this discussion is defined as the condition under which a farm has a negative farm net cash income and a debt/asset ratio above 40%. Farm businesses with these characteristics are vulnerable and likely to fail unless heavily subsidized by off-farm income, debt forgiveness, interest write-down, etc.

In 1986 the share of all farms in Ohio experiencing financial stress (13%) was slightly higher than the share of farms with financial stress in the Corn Belt region of the U.S. Conversely, a slightly lower percentage (87%) of Ohio farms was categorized as not stressed or vulnerable. This does not mean, however, that 87% of the farms were financially sound. It is important to realize that only one-half (50%) of all farms were in favorable financial condition; that is, they reported positive farm net cash income and a debt/asset ratio of .4 or less. The remaining 37% of Ohio farms, those that reported either a negative farm net cash income or a debt/asset ratio above .4, are not in imminent financial danger, but must judiciously consider business adjustments that will improve cash flow or reduce risk. Failure to do so will likely jeopardize the survivability of the farm business. The marginal financial condition of these farms is caused twice as often by negative cash flow as it is by excessive debt/asset ratio. This is cause for concern because of the short-run implications of not being able to meet cash commitments. These farms can become economic casualties very quickly.

Table 1. Farm Financial Condition*
December 1986

Financial Condition	Ohio	Corn Belt	U.S.
	------ percent of farms ------		
Favorable	50	50	57
Marginal Solvency	12	14	12
Marginal Income	25	25	21
Vulnerable	13	11	10

* Favorable: Positive farm net cash, debt/asset ratio .4 or below.
Marginal Solvency: Positive farm net cash, debt/asset ratio above .4.
Marginal Income: Negative farm net cash, debt/asset ratio .4 or below.
Vulnerable: Negative farm net cash, debt/asset ratio above .4.

Stressed (vulnerable) farms were found in all sales categories, although the below-$40,000 sales class, as may be expected, had the highest share of farms with stress. It is significant to note the declining proportion of farms in vulnerable financial condition as farm size increased. Large commercial farms (sales above $250,000) were only 1/3 as likely to be financially stressed as were medium size commercial farms ($40,000 to $250,000 sales) or small non-commercial farms.

The decline in the frequency of negative farm net cash flow, relative to farm size, was even more dramatic. Only 8% of the largest farms reported a negative cash flow, whereas this condition was four times as common (23%) on middle size farms and six times as frequent (48%) on small farms. Thirty-eight percent (38%) of all farms reported liquidity problems in 1986. However, it is important to remember that most of these were small farms. The middle and large size farms reported burdensome debt/asset ratios more frequently than small farms. Approximately 40% of the commercial farms (sales over $40,000) had debt/asset ratios exceeding 40%. These farms have limited risk-bearing capacity and need to reconsider their use of debt in the financial structure of their farm business.

Livestock farms--more specifically beef, hog, and sheep--exhibited a lower frequency of stress (7%) than either cash grain or dairy farms. This was, however, largely due to the lower frequency of debt/asset ratios above 40%. While nearly 1/3 of the cash grain and dairy farms reported high debt/asset ratios, only 12% of the beef, hog, and sheep farms did so. On the other hand, liquidity problems were most common (43%) on the beef, hog, and sheep operations. Cash grain farms were marginally better off from a liquidity perspective. Dairy farms, however, reported cash flow problems only half as often as cash grain or beef, hog, and sheep farms.

Table 2. Financial Vulnerability
Ohio, December 1986

	Percent of Farms With			
Farm Description	Zero Debt	Negative Cash Flow (A)	Debt/Asset Ratio Above .4 (B)	Both A and B
Farm Type				
Cash Grain	34	38	30	16
Beef, Hog, Sheep	52	43	12	7
Dairy	25	20	32	13
Farm Size (Sales)				
Above $250,000	10	8	35	4
$40,000-$250,000	17	23	40	11
Below $40,000	53	48	16	13
All Farms	39	38	25	13

Approximately 40% of the farms surveyed in Ohio ended 1986 with no debt outstanding. This is misleading, however, relative to larger commercial farms. Only 10% of the largest and 17% of the middle size commercial farms were debt-free, whereas 53% of the small part-time farms had no debt. Debt-free farming was most common on beef, hog, and sheep farms (52%). Approximately 1/3 of the cash grain farms and 1/4 of the dairy farms had no debt at the end of 1986. These farms, because cash is not required for debt service, are likely building cash reserves. They are or will be in a position to capitalize upon expansion opportunities that become available.

Prepared by:

Allan E. Lines, Extension Economist
The Ohio State University
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